

Bancorp, Inc.  
Form 10-Q  
November 09, 2006

---

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

---

**FORM 10-Q**

---

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended: September 30, 2006

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OF 15(d) OR THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from:            to

Commission file number: 51018

---

**THE BANCORP, INC.**

*(Exact name of registrant as specified in its charter)*

---

**Delaware**  
*(State or other jurisdiction of  
incorporation or organization)*

**405 Silverside Road**  
**Wilmington, DE 19809**

**23-3016517**  
*(IRS Employer  
Identification No.)*

Edgar Filing: Bancorp, Inc. - Form 10-Q

*(Address of principal executive offices) (Zip code)*

**Registrant's telephone number, including area code: (302) 385-5000**

---

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

(Check one): Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

As of November 3, 2006 there were 13,703,437 outstanding shares of Common Stock, \$1.00 par value.

---

**PART I FINANCIAL INFORMATION**

## Item 1. Financial statements

**The Bancorp, Inc. and Subsidiary****Consolidated Balance Sheets**

	September 2006 (unaudited)	December 31, 2005
	(in thousands)	
<b>ASSETS</b>		
Cash and cash equivalents		
Cash and due from banks	\$ 16,431	\$ 26,627
Interest bearing deposits	1,030	1,029
Federal funds sold	156,222	89,437
<b>Total cash and cash equivalents</b>	<b>173,683</b>	<b>117,093</b>
Investment securities, available-for-sale	115,477	103,596
Loans and Leases held for sale	467	805
Loans, net of deferred loan costs	947,034	680,777
Allowance for loan and lease losses	(7,583)	(5,513)
<b>Loans, net</b>	<b>939,451</b>	<b>675,264</b>
Premises and equipment, net	3,692	3,848
Accrued interest receivable	6,618	4,840
Goodwill	3,951	3,951
Other assets	9,725	8,074
<b>Total assets</b>	<b>\$ 1,253,064</b>	<b>\$ 917,471</b>
<b>LIABILITIES</b>		
Deposits		
Demand (non-interest bearing)	\$ 73,555	\$ 94,266
Savings, money market and interest checking	436,312	373,560
Time deposits	490,877	255,178
Time deposits, \$100,000 and over	20,723	9,584
<b>Total deposits</b>	<b>1,021,467</b>	<b>732,588</b>
Securities sold under agreements to repurchase	6,181	6,908
Federal Home Loan Bank advances	75,000	40,000
Accrued interest payable	3,770	778
Other liabilities	1,221	2,250
<b>Total liabilities</b>	<b>1,107,639</b>	<b>782,524</b>
<b>SHAREHOLDERS EQUITY</b>		
Preferred stock - authorized 5,000,000 shares of \$0.01 par value; issued and outstanding, 118,628 and 133,031 shares for September 30, 2006 and December 31, 2005, respectively	1	2
Common stock - authorized, 20,000,000 shares of \$1.00 par value; issued shares 13,703,437 and 13,637,148 for September 30, 2006 and December 31, 2005, respectively	13,703	13,637
Additional paid-in capital	125,292	124,278
Retained earnings	7,706	(1,544)

Edgar Filing: Bancorp, Inc. - Form 10-Q

Accumulated other comprehensive loss	(1,277)	(1,426)
Total shareholders' equity	145,425	134,947
Total liabilities and shareholders' equity	\$ 1,253,064	\$ 917,471

The accompanying notes are an integral part of these statements.

## The Bancorp Inc. and Subsidiary

## Consolidated Statements of Income

	For the three months		For the nine months	
	ended September 30, 2006	ended September 30, 2005	ended September 30, 2006	ended September 30, 2005
	(unaudited)			
	(in thousands, except share data)			
<b>Interest income</b>				
Loans, including fees	\$ 19,329	\$ 11,039	\$ 50,118	\$ 28,124
Investment securities	1,708	1,481	4,881	3,787
Federal funds sold and interest bearing deposits	802	294	2,311	880
	21,839	12,814	57,310	32,791
<b>Interest expense</b>				
Deposits	9,991	3,632	23,436	8,962
Securities sold under agreements to repurchase	20	18	42	59
Federal Home Loan Bank advances	543	409	1,513	1,045
Subordinated debt				138
	10,554	4,059	24,991	10,204
Net interest income	11,285	8,755	32,319	22,587
Provision for loan and lease losses	825	550	2,125	1,600
Net interest income after provision for loan and lease losses	10,460	8,205	30,194	20,987
<b>Non-interest income</b>				
Service fees on deposit accounts	224	185	609	518
Merchant credit card deposit fees	278	246	861	827
Gain on sales of investment securities				67
Leasing income	227	273	1,032	1,126
ACH Processing Fees	149	90	475	166
Other	211	176	845	571
Total non-interest income	1,089	970	3,822	3,275
<b>Non-interest expense</b>				
Salaries and employee benefits	2,960	2,754	9,302	7,745
Occupancy expense	673	599	1,995	1,749
Data processing expense	570	394	1,781	1,018
Advertising	117	178	415	448
Professional fees	492	414	1,276	955
Other	1,379	1,276	4,288	3,558
Prepayment premium on subordinated debt				1,285
Total non-interest expense	6,191	5,615	19,057	16,978
Net income before income tax	5,358	3,560	14,959	7,284
Income tax	2,074	1,254	5,652	2,750
Net income	3,284	2,306	9,307	4,754

Edgar Filing: Bancorp, Inc. - Form 10-Q

Less preferred stock dividends and accretion	(29)	(170)	(83)	(578)
Less preferred stock conversion premium		(459)		(459)
Income allocated to Series A preferred shareholders	(17)	(21)	(57)	(45)
Net income available to common shareholders	\$ 3,238	\$ 1,656	\$ 9,167	\$ 3,672
Net income per share - basic	\$ 0.24	\$ 0.12	\$ 0.67	\$ 0.29
Net income per share - diluted	\$ 0.23	\$ 0.12	\$ 0.64	\$ 0.28
Weighted average shares - basic	13,685,520	12,917,879	13,662,718	12,540,093
Weighted average shares - diluted	14,341,277	13,426,497	14,273,151	12,948,421

The accompanying notes are an integral part of these statements.

## The Bancorp, Inc. and Subsidiary

## Statements of Changes in Shareholders' Equity

For the three months ended September 30, 2006 (unaudited) and for the year ended December 31, 2005

	Common	Preferred	Additional	Retained	Accumulated		
	Stock	Stock	paid-in	Earnings	other	Comprehensive	
	Stock	Stock	capital	(Accumulated	comprehensive	income	Total
				deficit)	loss		
Balance at December 31, 2004	\$ 11,888	\$ 11	\$ 117,668	\$ (7,934)	\$ (231)		\$ 121,402
Net Income				7,447		7,447	7,447
Common Stock issued during the acquisition of Mears Leasing	253		3,716				3,969
Preferred Shares converted to Common Shares	1,000	(9)	(991)				
Common Stock issued from option exercise	26		239				265
Common Stock issued from warrant exercise	470		3,531				4,001
Cash dividends on Series A preferred stock				(942)			(942)
Accretion of Series A Preferred Stock			115	(115)			
Other comprehensive loss, net of reclassification adjustments and tax					(1,195)	(1,195)	(1,195)
Total other comprehensive income						\$ 6,252	
Balance at December 31, 2005	13,637	2	124,278	(1,544)	(1,426)		134,947
Net Income				9,307		9,307	9,307
Preferred Shares converted to Common Shares	14	(1)	(13)				
Common Stock issued from option exercise	52		797				849
Cash dividends on Series A preferred stock				(57)			(57)
Stock-based compensation			230				230
Other comprehensive income, net of reclassification adjustments and tax					149	149	149
						\$ 9,456	
Balance at September 30, 2006 (unaudited)	\$ 13,703	\$ 1	\$ 125,292	\$ 7,706	\$ (1,277)		\$ 145,425

The accompanying notes are an integral part of these statements.

## The Bancorp, Inc. and Subsidiary

## Statements of Cash Flows

(in thousands)

(unaudited)

For the nine months ended

	September 30,	
	2006	2005
Operating activities		
Net income	\$ 9,307	\$ 4,754
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	1,502	1,131
Provision for loan and lease losses	2,125	1,600
Net amortization (accretions) of premium (discount)	(10)	(59)
Net gain on sales of investment securities		(67)
Share based compensation expense	230	
Increase in accrued interest receivable	(1,778)	(163)
Increase in interest payable	2,992	294
Decrease (increase) in other assets	(786)	86
(Decrease) increase in other liabilities	(2,417)	19
Net cash provided by operating activities	11,165	7,595
Investing activities		
Purchase of investment securities	(11,649)	(30,208)
Proceeds from sales of investment securities	4	2,159
Proceeds from calls/maturity of investment securities		42,165
Cash paid in excess of cash equivalents from acquisition		(666)
Purchase of loans	(6,455)	
Net increase in loans	(259,518)	(180,243)
Purchases of premises and equipment	(901)	(1,542)
Net cash used in investing activities	(278,519)	(168,335)
Financing activities		
Net increase in deposits	288,879	269,622
Net increase in securities sold under agreements to repurchase	(727)	494
Net increase (decrease) from Federal Home Loan advances	35,000	(15,000)
Repayment of notes payable		(5,026)
Dividends on Series A preferred stock	(57)	(922)
Net proceeds from the exercise of options	685	239
Net proceeds from exercise of warrants		4,001
Excess Tax benefit from share based payment arrangements	164	
Redemption of subordinated debentures		(5,250)
Net cash provided by financing activities	323,944	248,158
Net increase in cash and cash equivalents	56,590	87,418
Cash and cash equivalents, beginning of year	117,093	19,503
Cash and cash equivalents, end of period	\$ 173,683	\$ 106,921



Edgar Filing: Bancorp, Inc. - Form 10-Q

Supplemental disclosure:		
Interest Paid	\$ 21,999	\$ 9,910
Taxes Paid	\$ 8,337	\$ 1,775

The accompanying notes are an integral part of these statements.

---

THE BANCORP, INC. AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

**Note 1. Significant Accounting Policies**

Basis of Presentation

The financial statements of The Bancorp, Inc. (Company) as of September 30, 2006 and for the three and nine month periods ended September 30, 2006 and 2005 are unaudited. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted in this Form 10-Q pursuant to the rules and regulations of the Securities and Exchange Commission. However, in the opinion of management, these interim financial statements include all necessary adjustments to fairly present the results of the interim periods presented. The unaudited interim consolidated financial statements should be read in conjunction with the audited financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005. The results of operations for the three and nine month periods ended September 30, 2006 may not necessarily be indicative of the results of operations for the full year ending December 31, 2006.

**Note 2. Stock-based Compensation**

The Company adopted Statement of Financial Accounting Standards (SFAS) No. 123(R) on January 1, 2006 using the modified prospective application method of transition. Prior to January 1, 2006, the Company followed Accounting Principles Bulletin (APB) No. 25 and the disclosure requirement of SFAS 123(R) with *pro forma* disclosures of net income and earnings per share, as if the fair value-based method of accounting defined in SFAS 123(R) has been applied. The Company's consolidated financial statement as of and for the third quarter of 2006 reflect the impact of adopting SFAS 123(R). In accordance with the modified prospective method, the consolidated financial statements for prior periods have not been restated to reflect, and do not include, the impact of SFAS 123(R).

At January 1, 2006, the Company recognized compensation expense for the portion of outstanding awards at January 1, 2006 for which the requisite service had not yet been rendered, based on the grant-date fair value of those awards calculated under SFAS 123 for *pro forma* disclosures. For new grants awarded on or after January 1, 2006, the Company has chosen to continue the use of the Black-Scholes option-pricing model (as used under SFAS 123) to estimate the fair value of each option on the date of grant. In accordance with SFAS 123(R), commencing January 1, 2006, the Company estimates the number of options for which the requisite service is expected to be rendered as compared to accounting for forfeitures as they occurred under SFAS 123. The Company has chosen to recognize compensation expense for new grants using the straight-line method over the vesting period.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions based on historical data used for grants at September 30, 2006 and September 30, 2005, respectively: expected volatility of 27.48% and 38%; risk-free interest rate of 4.57% and 4.26%; and an expected life of 7 years and 10 years. Expected volatility is based on the historical volatility of the Company's stock and peer group comparisons over the expected life of the grant. The risk-free rate for periods within the expected life of the option is based on the U.S. Treasury strip rate in effect at the time of the grant. The life of the option is based on historical factors which include the contractual term, vesting period, exercise behavior and employee terminations. In accordance with SFAS 123(R), stock based compensation expense for the nine months ended September 30, 2006 is based on awards that are ultimately expected to vest and therefore has been reduced for estimated forfeitures. The Company estimates forfeitures using historical data based upon the groups identified by management. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provision of SFAS No. 123(R) to stock-based employee compensation (in thousands).

Edgar Filing: Bancorp, Inc. - Form 10-Q

	For the three months ended September 30, 2005	For the nine months ended September 30, 2005
Net income, as reported	\$ 2,306	\$ 4,754
Add stock-based compensation expense included in reported net income, net of related tax effects	\$ 12	\$ 12
Less stock-based compensation costs under fair value based method for all awards	(55)	(1,838)
Pro forma net (loss) income	2,263	2,928
Less preferred stock dividends and accretion	(171)	(579)
Less preferred stock conversion premium	(459)	(459)
Income allocated to Series A preferred shareholders	(21)	(45)
Net (loss) income available to common shareholders	\$ 1,612	\$ 1,845
Net (loss) income per share basic, as reported	\$ 0.12	\$ 0.29
Net (loss) income per share basic, pro forma	\$ 0.12	\$ 0.15
Net (loss) income per share diluted, as reported	\$ 0.12	\$ 0.28
Net (loss) income per share diluted, pro forma	\$ 0.12	\$ 0.14

There is no pro forma effect for the nine months ended September 30, 2006 since stock based compensation was recorded under SFAS 123(R) in 2006.

The following table is a summary of the activity in the plans for the nine months ended September 30, 2006 and changes during the period:

	Shares	Weighted- Average Exercise Price	Average Remaining Contractual Years	Aggregate Intrinsic Value
Outstanding at beginning of the year	1,673,380	\$ 12.20		
Granted	1,000	\$ 20.98		
Exercised	51,886	\$ 13.23		
Forfeited		\$		
Outstanding at end of period	1,622,494	\$ 12.17	6.88	\$ 21,611,620
Options exercisable at end of period	1,572,744	\$ 12.12	8.45	\$ 21,027,587

The weighted-average grant-date fair value of options granted during the nine months ended September 30, 2006 and 2005 was \$8.45 and \$8.06 respectively. The total intrinsic value of options exercised during the third quarter 2006 and 2005 was \$208,000 and \$0, respectively. The total intrinsic value of options exercised during the nine months ended September 30, 2006 and 2005 were \$348,000 and \$0, respectively. Intrinsic value is measured using the fair market value price of the Company's common stock on the date of exercise less the applicable exercise price.



## Edgar Filing: Bancorp, Inc. - Form 10-Q

As of September 30, 2006, there was a total of \$133,000 of unrecognized compensation cost related to nonvested awards under share-based plans. This cost is expected to be recognized over a weighted average period of 1.13 years.

During the first quarter of 2006 the Company granted 13,500 phantom stock units that vest on December 31, 2006. Each stock unit represents the right to receive one share of common stock of the Company at the time the unit is fully vested. The fair value of the grants was \$17.50, which was the fair value of the common stock on the date of the grant. As of September 30, 2006 there was a total of \$63,000 of unrecognized compensation cost related to unvested phantom stock units. This cost is expected to be recognized over a weighted average period of 0.25 years.

### Note 3. Earnings Per Share

*Basic earnings per share* for a particular period of time is calculated by dividing net income by the weighted average number of common shares outstanding during that period.

*Diluted earnings per share* is calculated by dividing net income by the weighted average number of common shares and common share equivalents. The Company's only outstanding common share equivalents are options to purchase its common stock.

The following table shows the Company's earnings per share for the periods presented:

	For the three months ended September 30, 2006		
	Income	Shares	Per share
	(numerator)	(denominator) (dollars in thousands)	amount
<b>Basic earnings per share</b>			
Net income available to common shareholders	\$ 3,238	13,685,520	0.24
Effect of dilutive securities			
Options		651,881	(0.01)
Warrants			
Restricted Stock		3,876	

<b>Diluted earnings per share</b>			
Net income available to common stockholders plus assumed conversions	\$ 3,238	14,341,277	\$ 0.23

	For the nine months ended September 30, 2006		
	Income	Shares	Per share
	(numerator)	(denominator) (dollars in thousands)	amount
<b>Basic earnings per share</b>			
Net income available to common shareholders	\$ 9,167	13,662,718	0.67
Effect of dilutive securities			
Options		607,328	(0.03)
Warrants			
Restricted Stock		3,105	

<b>Diluted earnings per share</b>			
Net income available to common stockholders plus assumed conversions	\$ 9,167	14,273,151	\$ 0.64

Edgar Filing: Bancorp, Inc. - Form 10-Q

	For the three months ended September 30, 2005		
	Income	Shares	Per share
	(numerator)	(denominator) (dollars in thousands)	amount
<b>Basic earnings per share</b>			
Net income available to common shareholders	\$ 1,656	12,917,879	\$ 0.12
<b>Effect of dilutive securities</b>			
Options		462,446	
Warrants		46,172	
<b>Diluted earnings per share</b>			
Net income available to common stockholders plus assumed conversions	\$ 1,656	13,426,497	\$ 0.12

	For the nine months ended September 30, 2005		
	Income	Shares	Per share
	(numerator)	(denominator) (dollars in thousands)	amount
<b>Basic earnings per share</b>			
Net income available to common shareholders	\$ 3,672	12,540,093	\$ 0.29
<b>Effect of dilutive securities</b>			
Options		368,841	(0.01)
Warrants		39,487	
<b>Diluted earnings per share</b>			
Net income available to common stockholders plus assumed conversions	\$ 3,672	12,948,421	\$ 0.28

Stock options for 40,000 shares at an exercise price of \$16.67 per share were outstanding for the nine months ended September 30, 2005 but were not included the weighted average shares because the exercise price was greater than the market price.

**Note 4. Investment securities**

The amortized cost, gross unrealized gains and losses, and fair values of the Company's investment securities available-for-sale at September 20, 2006 are summarized as follows (in thousands):

	September 30, 2006			
	Amortized	unrealized	unrealized	Fair
	cost	gains	losses	value
U.S. Government agency securities	\$ 59,948	\$	\$ (1,432)	\$ 58,516
Mortgage backed securities	5,958	41	(572)	5,427
Other securities	51,505	296	(267)	51,534
	\$ 117,411	\$ 337	\$ (2,271)	\$ 115,477

	December 31, 2005			
	Amortized	Gross	Gross	Fair
	cost	unrealized	unrealized	value

Edgar Filing: Bancorp, Inc. - Form 10-Q

		gains	losses	
U.S. Government agency securities	\$ 59,936	\$	\$ (1,559)	\$ 58,377
Mortgage backed securities	5,553	27	(565)	5,015
Other securities	40,268	242	(306)	40,204
	\$ 105,757	\$ 269	\$ (2,430)	\$ 103,596

Edgar Filing: Bancorp, Inc. - Form 10-Q

The amortized cost and fair value of the Company's investment securities available-for-sale at September 30, 2006, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized cost	Fair value
Due after one year through five years	59,948	58,516
Due after five years through ten years	3,438	3,389
Due after ten years	50,255	49,802
Federal Home Loan and Atlantic Central Bankers Bank stock	3,770	3,770
	\$ 117,411	\$ 115,477

**Note 5. Loans**

Major classifications of loans are as follows (in thousands):

	September 30 2006 Amount (unaudited)	December 31, 2005 Amount
Commercial	\$ 154,750	\$ 119,654
Commercial mortgage	287,719	190,153
Construction	245,338	168,149
Total commercial loans	687,807	477,956
Direct financing leases, net	93,447	81,162
Residential mortgage (1)	62,763	62,378
Consumer loans and others	104,174	61,017
	948,191	682,513
Deferred loan costs	(690)	(931)
Total loans, net of deferred loan costs	\$ 947,501	\$ 681,582

(1) Includes loans held for sale of \$467,000 at September 30, 2006 and \$805,000 at December 31, 2005.

**Note 6. Transactions with affiliates**

The Company paid \$0 and \$16,900 to Cohen Bros. & Company, d/b/a Cohen & Company (Cohen Bros.), for investment securities brokerage services performed for the nine months ended September 30, 2006 and 2005, respectively. The Chairman of the Company is the principal of Cohen Bros. Financial LLC which owns 100% of Cohen Bros. & Company. A member of the Company's Board of Directors is the Chief Operating Officer of Cohen Bros. & Company.

The Company entered into a sublease for office space in Philadelphia, Pennsylvania and a technical support agreement with RAIT Investment Trust (RAIT) commencing in October 2000. The agreement was amended in June 2006. The Chief Executive Officer of RAIT is the Chief Executive Officer of the Company. RAIT paid the Company \$49,500 and \$45,000 for technical support services for the nine months ended September 30, 2006 and 2005, respectively. RAIT paid the Company approximately \$285,000 for rent for the first nine months of 2006 and \$230,000 for the first nine months of 2005.





The Company entered into a sublease and a technical and telephone support agreement with respect to office space in Philadelphia, Pennsylvania with Cohen Bros. commencing in July 2002. Cohen Bros. paid the Company \$28,000 and \$54,600 for the nine months ended September 30, 2006 and 2005, respectively, for technical and telephone support services. Cohen Bros. paid approximately \$87,000 in rent for the nine months ended September 30, 2006 and \$88,000 for the first nine months ended September 30, 2005. In June 2006 Cohen Bros. terminated the sublease and technical support agreement.

The Company maintains deposits for various affiliated companies totaling approximately \$101,953,000 and \$115,942,000 as of September 30, 2006 and December 31, 2005, respectively. The majority of these deposits are short-term in nature and rates are consistent with market rates.

The Company has entered into lending transactions in the ordinary course of business with directors, executive officers, principal stockholders and affiliates of such persons on the same terms as those prevailing for comparable transactions with other borrowers. At September 30, 2006, these loans were current as to principal and interest payments and, in the opinion of management, do not involve more than normal risk of collectibility. At September 30, 2006 loans to these related parties amounted to \$2,992,212 in outstanding principal amount.

#### **Note 7. Reclassifications**

Certain prior period amounts have been reclassified to conform to the current year's presentation.

#### **Note 8. Repayment of Subordinated Debentures**

In March 2005, the Bancorp Capital Trust redeemed its trust preferred securities at their face value including accrued interest through March 31, 2005 and a prepayment premium representing the discounted present value of dividends payable on the trust preferred securities through September 12, 2007, the date the Company could call these securities. The proceeds for the redemption came from the Company's redemption of its subordinated debenture to the Bancorp Capital Trust. The aggregate redemption price was \$6.1 million. The Company recorded an expense of approximately \$1.3 million for the three months ended March 31, 2005, reflecting a prepayment premium of \$819,000 and the remaining unamortized offering expenses of \$466,000.

#### **Note 9. New Accounting Pronouncement**

In July 2006, the FASB issued FASB Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes* an interpretation of FASB Statement No. 109. FIN 48 requires that realization of an uncertain income tax position be more likely than not before it can be recognized in the financial statements. Further, FIN 48 prescribes the benefit to be recorded in the financial statements as the amount most likely to be realized assuming a review by tax authorities having all relevant information and applying current conventions. FIN 48 also clarifies the financial statement classification of tax-related penalties and interest and sets forth new disclosures regarding unrecognized tax benefits. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the requirements of FIN 48 and the impact this interpretation may have on its financial statements.

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets*. This Statement amends SFAS No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, and requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable, and permits the entities to elect either fair value measurement with changes in fair value reflected in earnings or the amortization and impairment requirements of SFAS No. 140 for subsequent measurement. The subsequent measurement of separately recognized servicing assets and servicing liabilities at fair value eliminates the necessity for entities that manage the risks inherent in servicing assets and servicing liabilities with derivatives to qualify for hedge accounting treatment and eliminates the characterization of declines in fair value as impairments or direct write-downs. This Statement is effective as of the beginning of an entity's first fiscal year that begins after September 15, 2006. The Company is evaluating the impact, if any, of the adoption of this Statement on its financial results.

In September 2006, the FASB issued SFAS No. 158, *Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans* (an amendment of FASB Statements No. 87, 88, 106, and 132R) (SFAS 158). SFAS 158 requires an employer to recognize in its statement of financial position an asset for a plan's over funded status or a liability for a plan's under funded status, measure a

plan's assets and its obligations that determine its funded status as of the end of the employer's fiscal year (with limited exceptions), and recognize changes in the funded status of a defined benefit postretirement plan in the year in which the changes occur. Those changes will be reported in our comprehensive income and as a separate component of shareholders' equity. SFAS 158 is effective for us in the fourth quarter of fiscal 2007. The Company is evaluating the impact, if any, of the adoption of this Statement on its financial results.

In September 2006, the SEC released SAB No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" (SAB No. 108), that provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. The SEC staff believes that registrants should quantify errors using both a balance sheet and an income statement approach and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. This pronouncement is effective for fiscal years ending after November 15, 2006. The Company believes the adoption of SAB No. 108 will have no material impact on its financial position, results of operations, or cash flows.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (SFAS No. 157). This statement provides a single definition of fair value, a framework for measuring fair value, and expanded disclosures concerning fair value. Previously, different definitions of fair value were contained in various accounting pronouncements creating inconsistencies in measurement and disclosures. SFAS No. 157 applies under those previously issued pronouncements that prescribe fair value as the relevant measure of value, except SFAS No. 123(R) and related interpretations and pronouncements that require or permit measurement similar to fair value but are not intended to measure fair value. This pronouncement is effective for fiscal years beginning after November 15, 2007. The Company is evaluating the impact of this new standard, but currently believes that adoption will not have a material impact on its financial position, results of operations, or cash flows.

---

**Part I - Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION**

*Forward-Looking Statements*

*When used in this Form 10-Q, the words believes anticipates expects and similar expressions are intended to identify forward-looking statements. Such statements are subject to certain risks and uncertainties more particularly described in Item 1, under the caption Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2005. These risks and uncertainties could cause actual results to differ materially. Readers are cautioned not place undue reliance on these forward-looking statements, which speak only as of the date hereof. We undertake no obligation to publicly release the results of any revisions to forward-looking statements which we may make to reflect events or circumstances after the date of this Quarterly Report on Form 10-Q or to reflect the occurrence of unanticipated events.*

*In the following discussion we provide information about our results of operations, financial condition, liquidity and asset quality. We intend that this information facilitate your understanding and assessment of significant changes and trends related to our financial condition and results of operations. You should read this section in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operation included in our Annual Report on Form 10-K for the year ended December 31, 2005.*

**Critical Accounting Policies and Estimates**

Our accounting and reporting policies conform with accounting principles generally accepted in the United States and general practices within the financial services industry. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results could differ from those estimates.

We believe that the determination of our allowance for loan and lease losses involves a higher degree of judgment and complexity than our other significant accounting policies. We determine our allowance for loan and lease losses with the objective of maintaining a reserve level we believe to be sufficient to absorb our estimated probable credit losses. We base our determination of the adequacy of the allowance on periodic evaluations of our loan portfolio and other relevant factors. However, this evaluation is inherently subjective as it requires material estimates, including, among others, expected default probabilities, the amount of loss we may incur on a defaulted loan, expected commitment usage, the amounts and timing of expected future cash flows on impaired loans, value of collateral, estimated losses on consumer loans and residential mortgages, and historical loss experience. We also evaluate economic conditions, uncertainties in estimating losses and inherent risks in the loan portfolio. All of these factors may be susceptible to significant change. To the extent actual outcomes differ from our estimates, we may need additional provisions for loan losses that would adversely impact our earnings.

Beginning in January 2006, we adopted the provisions of SFAS 123R, which requires the expense recognition for the fair value of share based compensation awards, such as stock options, restricted stock, performance based shares and the like. This standard allows management to establish modeling assumptions as to expected stock price volatility, option terms, forfeiture rates and dividend rates which directly impact estimated fair value. All of these estimates and assumptions may be susceptible to significant change that may impact earnings in future periods.

We capitalize costs associated with internally developed and purchased software systems for new products and enhancements to existing products that have reached the application stage and meet recoverability tests. Capitalized costs include external direct costs of materials and services used in developing or obtaining internal-use software, payroll and payroll related expenses for employees who are directly associated with and devote time to internal-use software projects and interest costs incurred, if material, while developing internal-use software. Capitalization of these costs begins when we complete the preliminary project stage, and ceases no later than the point at which the project is substantially complete and ready for its intended purpose.

We account for income taxes under the liability method whereby we determine deferred tax assets and liabilities based on the difference between the carrying values on our financial statements and the tax basis of assets and liabilities as measured by the enacted tax rates which will be in effect when these differences reverse. Deferred tax expense (benefit) is the result of changes in deferred tax assets and liabilities.

**Results of Operations****Third quarter 2006 to third quarter 2005**

**Net Income:** Net income for the third quarter of 2006 was \$3.3 million, compared to net income of \$2.3 million for the third quarter of 2005. Diluted earnings per share were \$0.23 in the third quarter of 2006 as compared to \$0.12 for the third quarter of 2005. Return on average assets was 1.20% and return on average equity was 9.30% for the third quarter of 2006, as compared to 1.22% and 6.96%, respectively, for the third quarter of 2005.

**Net Interest Income:** Our interest income for the third quarter of 2006 increased to \$21.8 million from \$12.8 million in the third quarter of 2005, while our net interest income increased to \$11.3 million from \$8.8 million. Our average loans increased to \$899.4 million for the third quarter of 2006 from \$583.1 million for the third quarter of 2005. The primary reason for the increases in our interest income and net interest income was our ability to increase our earning assets through continued organic growth of our loan portfolio.

Our net interest margin for the third quarter 2006 decreased to 4.21% from 4.77% for the third quarter of 2005, a decrease of 56 basis points (.56%). The decreased net interest margin resulted from the following:

deposit and short-term borrowing rates are increasing more rapidly than loan rates, and

the impact of a flattening yield curve.

In general, changes in rates immediately affect our variable rate loans, while deposit rates tend to take a longer period to adjust, which in general would mean the Company is considered to have an asset sensitive balance sheet. In a rising rate environment this would typically lead to an improving net interest margin; however, the current interest rate environment is causing liabilities to reprice over a shorter period of time. Management attributes this principally to a highly competitive deposit pricing environment. Additionally, the Company's mix of deposits has shifted to include a higher proportion of certificates of deposit, which generally carry a higher interest rate cost than other types of interest-bearing deposits. For the third quarter of 2006, the average yield on our interest-earning assets increased to 8.16% from 6.98% for third quarter of 2005, an increase of 118 basis points (1.18%). Cost of interest-bearing deposits increased to 4.84% for the third quarter of 2006 from 3.07% for the third quarter of 2005, an increase of 176 basis points (1.76%). Average interest bearing deposits increased to \$827.9 million from \$472.6 million, an increase of \$355.3 million or 75.2%.

**Average Daily Balances.** The following table presents the average daily balances of assets, liabilities and stockholders' equity and the respective interest earned or paid on interest-earning assets and interest-bearing liabilities, as well as average rates, for the periods indicated:

	Three Months ended September 30,					
	2006			2005		
	Average Balance	Interest	Rate	Average Balance	Interest	Rate
(dollars in thousands)						
<b>Assets:</b>						
Interest-earning assets:						
Loans net of unearned discount	\$ 899,376	\$ 19,329	8.60%	\$ 583,119	\$ 11,039	7.57%
Investment securities	113,352	\$ 1,708	6.03%	107,112	1,481	5.53%
Interest bearing deposits	1,030		0.00%	1,029	1	0.39%
Federal funds sold	57,301	802	5.60%	43,474	293	2.70%
Net interest-earning assets	1,071,059	21,839	8.16%	734,734	12,814	6.98%
Allowance for loan and lease losses	(7,022)			(4,805)		
Other assets	33,201			27,369		
	\$ 1,097,238			\$ 757,298		

Edgar Filing: Bancorp, Inc. - Form 10-Q

<b>Liabilities and Shareholders Equity:</b>									
Deposits:									
Demand (non-interest bearing)	\$	79,954			\$	101,933			
Interest bearing deposits									
Interest checking		63,650	\$	411	2.58%	28,384	\$	88	1.24%
Savings and money market		320,641		3,939	4.91%	205,183		1,473	2.87%
Time		443,585		5,641	5.09%	239,012		2,071	3.47%
Total interest bearing deposits		827,876		9,991	4.83%	472,579		3,632	3.07%
FHLB advances		38,780		543	5.61%	44,076		409	3.71%
Other borrowed funds		4,985		20	1.60%	4,102		18	1.76%
Subordinated debt									
Net interest bearing liabilities		871,641		10,554	4.84%	520,757		4,059	3.12%
Other liabilities		4,357				2,109			
Shareholders equity		141,286				132,499			
	\$	1,097,238				\$	757,298		
Net yield on average interest earning assets			\$	11,285	4.21%		\$	8,755	4.77%

In the third quarter of 2006, average interest-earning assets increased to \$1.1 billion, an increase of \$336.3 million, or 45.8%, from the third quarter of 2005.

*Provision for Loan and Lease Losses.* Our provision for loan and lease losses was \$825,000 for the third quarter of 2006 compared to \$550,000 for the third quarter of 2005. For more information about our provisions and allowance for loan and lease losses and our loss experience see Allowance for Loan and Lease Losses and Summary of Loan and Lease Loss Experience, below.

*Non-Interest Income.* Non-interest income was \$1.1 million for the third quarter of 2006 as compared to \$970,000 for the third quarter of 2005, an increase of \$119,000 or 12.3%. The principal reasons for the increase in non-interest income were an increase in income from Automated Clearing House (ACH) processing fees and an increase in other income. Our ACH processing fees increased to \$149,000 for the third quarter of 2006, an increase of \$59,000 or 65.6% as a result of organic growth as more customers convert to ACH processing. Service fees on deposit accounts increased to \$224,000 in the third quarter of 2006 from \$185,000, an increase of \$39,000 or 21.1%. The increase in fees charged to accounts is a result of the increasing number of health savings accounts which carry substantially higher fees than basic deposit accounts. Leasing income decreased to \$227,000 from \$273,000, a decrease of \$46,000 or 16.8%. The decrease in income is due to the effect of rising fuel prices on the resale value of commercial vehicles in the secondary market. Approximately 94% of our lease portfolio, by cost, consists of automobile leases.

*Non-Interest Expense.* Total non-interest expense was \$6.2 million for the third quarter of 2006, as compared to \$5.8 million for third quarter of 2005, an increase of \$576,000 million or 10.3%. Salaries and employee benefits amounted to \$3.0 million for the third quarter of 2006 as compared to \$2.9 million for the third quarter of 2005. The increase in salaries and employee benefits resulted from increases in the commercial lending and affinity group staffs relating to the growth in our loan portfolio and our private client and health savings account lines of business. Computer expense increased to \$570,000 for the third quarter of 2006 an increase of \$176,000 or 44.7%. The increase reflects the upgrade of our internet banking platform in 2005 and increases from growth in the health savings account portfolio. Professional fees increased to \$492,000 for the third quarter of 2006, an increase of \$78,000 or 18.8%. The increase reflects the increasing compliance costs that are associated with being a public company, in particular the costs associated with compliance with the Sarbanes-Oxley Act of 2002.

***First nine months of 2006 to first nine months of 2005***

*Net Income:* Net income for the first nine months of 2006 was \$9.3 million, compared to net income of \$4.8 million for the first nine months of 2005. Diluted earnings per share were \$0.64 in the first nine months of 2006 as compared to \$0.28 for the first nine months of 2005. Return on average assets was 1.24% and return on average equity was 8.97% for first nine months of 2006, as compared to .90% and 4.96%, respectively for the first nine months of 2005.

## Edgar Filing: Bancorp, Inc. - Form 10-Q

*Net Interest Income:* Our interest income for the first nine months of 2006 increased to \$57.3 million from \$32.8 million in the first nine months of 2005, while our net interest income increased to \$32.3 million from \$22.6 million. Our average loans increased to \$802.1 million for first nine months of 2006 from \$522.9 million for the first nine months of 2005. As stated above, the primary reason for the increases in our interest income and net interest income was our ability to increase our earning assets through continued organic growth of our loan portfolio.

Our net interest margin for the first nine months 2006 increased to 4.41% from 4.47% for the first nine months of 2005, a decrease of 6 basis points (.06%). The decreased net interest margin resulted from the following:

deposit and short-term borrowing rates are increasing more rapidly than loan rates, and

the impact of a flattening yield curve.

In the first nine months of 2006, the average yield on our interest-earning assets increased to 7.83% from 6.50% for first nine months of 2005 an increase of 133 basis points (1.33%). Cost of interest-bearing deposits increased to 4.31% for the first nine months of 2006 from 2.73% for the first nine months of 2005, an increase of 158 basis points (1.58%). Average interest bearing deposits increased to \$724.3 million from \$438.2 million, an increase of \$286.1 million or 65.3%.

*Average Daily Balances.* The following table presents the average daily balances of assets, liabilities and stockholders' equity and the respective interest earned or paid on interest-earning assets and interest-bearing liabilities, as well as average rates, for the periods indicated:

	Nine Months ended September 30,					
	2006			2005		
	Average	Average	Average	Average	Average	Average
	Balance	Interest	Rate	Balance	Interest	Rate
(dollars in thousands)						
<b>Assets:</b>						
Interest-earning assets:						
Loans net of unearned discount	\$ 802,072	\$ 50,118	8.33%	\$ 522,862	\$ 28,124	7.17%
Investment securities	112,316	4,881	5.79%	106,871	3,787	4.72%
Interest bearing deposits	1,030	1	0.13%	1,029	2	0.26%
Federal funds sold	60,695	2,310	5.07%	42,285	878	2.77%
Net interest-earning assets	976,113	57,310	7.83%	673,047	32,791	6.50%
Allowance for loan and lease losses	(6,390)			(4,255)		
Other assets	34,987			32,177		
	\$ 1,004,710			\$ 700,969		
<b>Liabilities and Shareholders' Equity:</b>						
Deposits:						
Demand (non-interest bearing)	\$ 94,534			\$ 83,921		
Interest bearing deposits						
Interest checking	59,080	\$ 1,035	2.34%	27,182	\$ 232	1.14%
Savings and money market	309,216	10,064	4.34%	195,805	3,810	2.59%
Time	355,995	12,337	4.62%	215,243	4,920	3.05%
Total interest bearing deposits	724,291	23,436	4.31%	438,230	8,962	2.73%
FHLB advances	39,048	1,513	5.17%	44,451	1,045	3.13%
Other borrowed funds	4,132	42	1.36%	4,139	59	1.90%
Subordinated debt				1,750	138	10.51%



Edgar Filing: Bancorp, Inc. - Form 10-Q

Net interest bearing liabilities	767,471	24,991	4.34%	488,570	10,204	2.78%
Other liabilities	4,326			620		
Shareholders' equity	138,379			127,858		
	\$ 1,004,710			\$ 700,969		
Net yield on average interest earning assets		\$ 32,319	4.41%		\$ 22,587	4.47%

*Provision for Loan and Lease Losses.* Our provision for loan and lease losses was \$2.1 million for the first nine months of 2006 compared to \$1.6 million for the first nine months of 2005. For more information about our provisions and allowance for loan and lease losses and our loss experience see Allowance for Loan and Lease Losses and Summary of Loan and Lease Loss Experience, below.

*Non-Interest Income.* Non-interest income, exclusive of gains on sales of investment securities, was \$3.8 million for the first nine months of 2006 as compared to \$3.2 for the first nine months of 2005, an increase of \$614,000 or 19.1%. Gains on sales of investment securities totaled \$0 in the first nine months of 2006 compared to \$67,000 of gains on sale investment securities for the same period in 2005. The principal reasons for the increase in non-interest income was an increase in income from ACH processing fees as a result of organic growth as customers transition to ACH processing. ACH income increased to \$475,000 for the first nine months of 2006 from \$166,000, an increase of 309,000 or 186% from the same period last year. Leasing income decreased \$94,000 to \$1.0 million for first nine months of 2006 over the same period in 2005. The decrease in income is due to the effect of rising fuel prices on the resale value of commercial vehicles in the secondary market. Approximately 94% of our lease portfolio, by cost, consists of automobile leases. Other non-interest income was \$845,000 for the first nine months of 2006 as compared to \$571,000 over the same period in 2005. Approximately \$165,000 of the increase was a fee we received from MasterCard after its initial public offering.

*Non-Interest Expense.* Total non-interest expense was \$19.1 million for the first nine months of 2006, as compared to \$16.8 million for first nine months of 2005, an increase of \$2.3 million or 13.7%. Salaries and employee benefits amounted to \$9.3 million for the first nine months of 2006 as compared to \$7.7 million for the first nine months of 2005. The increase in salaries and employee benefits resulted from increases in the commercial lending and affinity group staffs relating to the growth in our loan portfolio and our private client and health savings account lines of business. Computer expense increased to \$1.8 million for the first nine months of 2006 an increase of \$763,000 or 75.0%. The increase reflects the upgrade of our internet banking platform in 2005 and increases from growth in our health savings account portfolio. Professional fees increased to \$1.3 million for the first nine months of 2006 an increase of \$321,000 or 33.6%. The increase reflects the increasing compliance costs that are associated with being a public company, in particular the costs associated with compliance with the Sarbanes-Oxley Act of 2002. In the first quarter of 2005, we redeemed our outstanding subordinated debentures at a premium of \$869,000. The redemption of the subordinated debentures, which supported our trust preferred securities, also resulted in the writing-off \$466,000 of the unamortized offering costs from the trust preferred securities offering in 2002. The total expense associated with the redemption of the subordinated debentures in the first quarter of 2005 was \$1.3 million. Other non-interest expense increased to \$4.3 million from \$3.6 million, an increase of \$730,000 or 20.5%. This increase is due primarily to increased printing costs and telephone expense as a result of growth in the health savings account line of business as well as an increase in insurance costs.

## **Liquidity and Capital Resources**

Liquidity defines our ability to generate funds to support asset growth, meet deposit withdrawals, satisfy borrowing needs and otherwise operate on an ongoing basis. We invest the funds we do not need for operation primarily in overnight federal funds.

The primary source of funds for our financing activities has been cash inflows from net increases in deposits, which were \$288.9 million in the nine months of 2006. We have also used sources outside of our core deposit products to fund our loan growth including Federal Home Loan Bank advances and repurchase agreements. As of September 30, 2006, we had \$75.0 million of outstanding Federal Home Loan Bank advances and \$6.2 million in repurchase agreements.

Funding was directed primarily at cash outflows required for loans, which were \$266.0 million in the first nine months of 2006. At September 30, 2006, we had outstanding commitments to fund loans, including unused lines of credit, of \$344.9 million.

## Edgar Filing: Bancorp, Inc. - Form 10-Q

We must comply with capital adequacy guidelines issued by the Federal Deposit Insurance Corporation, or FDIC. A bank must, in general, have a leverage ratio of 5.0%, a ratio of Tier I capital to risk-weighted assets of 6.0% and a ratio of total capital to risk-weighted assets of 10.0% in order to be considered well capitalized. A Tier I leverage ratio is the ratio of Tier 1 capital to average assets for the period. Tier I capital includes common shareholders' equity, certain qualifying perpetual preferred stock and minority interests in equity accounts of consolidated subsidiaries, less goodwill. At September 30, 2006 we were well capitalized under banking regulations.

The following table sets forth our regulatory capital amounts and ratios for the periods indicated:

	<b>Tier 1 capital to average assets ratio</b>	<b>Tier 1 capital to risk-weighted assets ratio</b>	<b>Total capital to risk-weighted assets ratio</b>
<b>AS OF SEPTEMBER 30, 2006</b>			
The Company	13.07%	13.37%	14.08%
The Bancorp Bank	12.04%	12.28%	12.99%
Well capitalized institution (under FDIC regulations)	5.00%	6.00%	10.00%
<b>AS OF DECEMBER 31, 2005:</b>			
The Company	15.90%	17.94%	18.69%
The Bancorp Bank	14.65%	16.46%	17.20%
Well capitalized institution (under FDIC regulations)	5.00%	6.00%	10.00%

---

**Asset and Liability Management**

The management of rate sensitive assets and liabilities is essential to controlling interest rate risk and optimizing interest margins. An interest rate sensitive asset or liability is one that, within a defined time period, either matures or experiences an interest rate change in line with general market rates. Interest rate sensitivity measures the relative volatility of a bank's interest margin resulting from changes in market interest rates.

We monitor and control interest rate risk through a variety of techniques, including use of traditional interest rate sensitivity analysis (also known as gap analysis). Traditional gap analysis involves arranging our interest-earning assets and interest-bearing liabilities by repricing periods and then computing the difference (or interest rate sensitivity gap) between the assets and liabilities that are estimated to reprice during each time period and cumulatively through the end of each time period.

Gap analysis requires estimates as to when individual categories of interest-sensitive assets and liabilities will reprice, and assumes that assets and liabilities assigned to the same repricing period will reprice at the same time and in the same amount. Gap analysis does not account for the fact that repricing of assets and liabilities is discretionary and subject to competitive and other pressures. A gap is considered positive when the amount of interest rate sensitive assets exceeds the amount of interest rate sensitive liabilities. A gap is considered negative when the amount of interest rate sensitive liabilities exceeds interest rate sensitive assets. During a period of falling interest rates, a positive gap would tend to adversely affect net interest income, while a negative gap would tend to result in an increase in net interest income. During a period of rising interest rates, a positive gap would tend to result in an increase in net interest income while a negative gap would tend to affect net interest income adversely.

The following table sets forth the estimated maturity/repricing structure of our interest-earning assets and interest-bearing liabilities at September 30, 2006. Except as stated below, the amounts of assets or liabilities shown which reprice or mature during a particular period were determined in accordance with the contractual terms of each asset or liability. The majority of interest-bearing demand deposits and savings deposits are assumed to be core deposits, or deposits that will generally remain with us regardless of market interest rates. Therefore, 50% of the core interest checking deposits and 25% of core savings and money market deposits are shown as maturing or repricing within the 1-90 days column with the remainder shown in the 1-3 years column. We estimate the repricing characteristics of these deposits based on historical performance, past experience at other institutions and other deposit behavior assumptions. However, we may choose not to reprice liabilities proportionally to changes in market interest rates for competitive or other reasons. Payments of fixed-rate loans and mortgage-backed securities are scheduled based on their anticipated cash flow, including prepayments based on historical data and current market trends. The table does not necessarily indicate the impact of general interest rate movements on our net interest income because the repricing of certain categories of assets and liabilities is beyond our control as, for example, prepayments of loans and withdrawal of deposits. As a result, certain assets and liabilities indicated as repricing within a stated period may in fact reprice at different times and at different rate levels.

Edgar Filing: Bancorp, Inc. - Form 10-Q

	1-90	91-364	1-3	3-5	Over 5
	Days	Days	Years	Years	Years
	(dollars in thousands)				
<b>Interest earning assets:</b>					
Loans net of unearned discount	\$ 531,741	\$ 75,558	\$ 177,823	\$ 84,338	\$ 78,041
Investments, available for sale		58,516	3,389	49,802	3,770
Interest bearing deposits	1,030				
Federal funds sold	156,222				
<b>Total interest earning assets</b>	<b>688,993</b>	<b>134,074</b>	<b>181,212</b>	<b>134,140</b>	<b>81,811</b>
<b>Interest bearing liabilities:</b>					
Interest checking	16,939		50,815		
Savings and money market	92,140		276,418		
Time deposits	220,264	265,878	25,351	107	
Securities sold under agreements to repurchase	6,181				
Federal Home Loan Bank advances	75,000				
<b>Total interest bearing liabilities</b>	<b>410,524</b>	<b>265,878</b>	<b>352,584</b>	<b>107</b>	
<b>Gap</b>	<b>\$ 278,469</b>	<b>\$ (131,804)</b>	<b>\$ (171,372)</b>	<b>\$ 134,033</b>	<b>\$ 81,811</b>
<b>Cumulative gap</b>	<b>\$ 278,469</b>	<b>\$ 146,665</b>	<b>\$ (24,707)</b>	<b>\$ 109,326</b>	<b>\$ 191,137</b>
Gap to assets ratio	22%	-11%	-14%	11%	7%
Cumulative gap to assets ratio	22%	12%	-2%	9%	15%

The method used to analyze interest rate sensitivity in this table has a number of limitations. Certain assets and liabilities may react differently to changes in interest rates even though they reprice or mature in the same or similar time periods. The interest rates on certain assets and liabilities may change at different times than changes in market interest rates, with some changing in advance of changes in market rates and some lagging behind changes in market rates. Additionally, the actual prepayments and withdrawals we experience when interest rates change may deviate significantly from those assumed in calculating the data shown in the table.

**Financial Condition**

*General.* Our total assets at September 30, 2006 were \$1.3 billion, of which our total loans were \$947.5 million. At December 31, 2005 our total assets were \$917.5 million, of which our total loans were \$681.6 million. Our portfolio of commercial, commercial mortgage and construction loans grew \$209.9 million, or 43.9%, from year-end 2005 to \$687.8 million at September 30, 2006. At September 30, 2006 our federal funds sold amounted to \$156.2 million as compared to \$89.4 million at December 31, 2005. The increase is the result of period end increases in deposits from payment processing and commercial customers; however the average federal funds balance for the third quarter of 2006 was \$57.3 million which was an increase of \$13.8 over the average balance for the third quarter of 2005.

*Investment portfolio.* For detailed information on the composition and maturity distribution of our investment portfolio, see Note 3 to the Notes to Financial Statements contained in this Quarterly Report on Form 10-Q. Total investment securities increased to \$115.5 million on September 30, 2006, an increase of \$11.9 million or 11.5% from year-end 2005. Investments increased primarily due to a \$10 million investment during the first quarter 2006.

*Loan Portfolio.* Total loans increased to \$947.5 million at September 30, 2006 from \$681.6 million at December 31, 2005, an increase of \$265.9 million or 39.01%.

Edgar Filing: Bancorp, Inc. - Form 10-Q

The following table summarizes our loan portfolio by loan category for the periods indicated (in thousands):

	September 30	December 31,
	2006	2005
	Amount (unaudited)	Amount
Commercial	\$ 154,750	\$ 119,654
Commercial mortgage	287,719	190,153
Construction	245,338	168,149
Total commercial loans	687,807	477,956
Direct financing leases, net	93,447	81,162
Residential mortgage (1)	62,763	62,378
Consumer loans and others	104,174	61,017
	948,191	682,513
Deferred loan costs	(690)	(931)
Total loans, net of deferred loan costs	\$ 947,501	\$ 681,582

(1) Includes loans held for sale of \$467,000 at September 30, 2006 and \$805,000 at December 31, 2005.

*Allowance for Loan and Lease Losses.* Management reviews the adequacy of our allowance for loan and lease losses on at least a quarterly basis to ensure that the provision for loan losses which we charge against earnings is in an amount necessary to maintain our allowance at a level that is appropriate, based on management's estimate of probable losses. Our estimates of loan and lease losses are intended to, and, in management's opinion, do, meet the criteria for accrual of loss contingencies in accordance with Statement of Financial Accounting Standards, or SFAS, No. 5, Accounting for Contingencies, and SFAS No. 114, as amended, Accounting by Creditors for Impairment of a Loan. The process of evaluating this adequacy has two basic elements: first, the identification of problem loans or leases based on current financial information and the fair value of the underlying collateral; and second, a methodology for estimating general loss reserves inherent in the portfolio. For loans or leases classified as special mention, substandard or doubtful, we record all estimated losses at the time we classify the loan or lease. This specific portion of the allowance is the total of potential, although unconfirmed, losses for individually classified loans. Because we immediately charge off all identified losses, no portion of the allowance for loan losses is restricted to any individual loan or groups of loans, and the entire allowance is available to absorb any and all loan losses.

The second phase of our analysis represents an allocation of the allowance. This methodology analyzes pools of loans that have similar characteristics and applies historical loss experience and other factors for each pool to determine its allocable portion of the allowance. This estimate is intended to represent the potential unconfirmed and inherent losses within the portfolio. Individual loan pools are created for major loan categories: commercial loans, commercial mortgages, construction loans and direct lease financing, and for the various types of loans to individuals. We augment our historical experience for each loan pool by accounting for such items as: current economic conditions, current loan portfolio performance, loan policy or management changes, loan concentrations, increases in our lending limit, the average loan size, and other factors as appropriate.

Although the performance of our loan portfolio has been above that of our peers, and we do not currently foresee a change in that performance, our analysis for purposes of deriving the historical loss component of the allowance includes factors in addition to our historical loss experience, such as management's experience with similar loan and lease portfolios at other institutions, the historic loss experience of our peers and statistical information from various industry reports such as the FDIC's Quarterly Banking Profile.

While we consider our allowance for loan and lease losses to be adequate based on information currently available, future additions to the allowance may be necessary due to changes in economic conditions or management's assumptions as to future delinquencies, recoveries and losses and management's intent with regard to the disposition of loans and leases. We review the adequacy of the allowance on at least a quarterly basis to ensure that the provision for loan and lease losses that has been charged against earnings is an amount necessary to maintain the allowance at a level that is appropriate based on management's assessment of probably estimated losses. The following table summarizes our credit loss experience for each of the periods indicated:



Edgar Filing: Bancorp, Inc. - Form 10-Q

	Nine months ended		For the year ended
	September 30, 2006	September 30, 2005 (dollars in thousands)	December 31, 2005
Balance in the allowance for loan and lease losses at beginning of period	\$ 5,513	\$ 3,593	\$ 3,593
Loans charged-off:			
Commercial		123	123
Lease financing	62	8	70
Consumer		2	2
Total	62	133	195
Recoveries:			
Lease financing	7	15	15
Total	7	15	15
Net charge-offs (recoveries)	55	118	180
Provision charged to operations	2,125	1,600	2,100
Balance in allowance for loan and lease losses at end of period	\$ 7,583	\$ 5,075	\$ 5,513

Net charge-offs/average loans	0.01%	0.02%	0.03%
-------------------------------	-------	-------	-------

*Non-Performing Loans.* Loans are considered to be non-performing if they are on a non-accrual basis or terms have been renegotiated to provide a reduction or deferral of interest or principal because of a weakening in the financial positions of the borrowers. A loan which is past due 90 days or more and still accruing interest remains on accrual status only when it is both adequately secured as to principal and is in the process of collection. We had \$0 non-accrual or renegotiated loans at September 30, 2006 compared to \$0 of non-accrual loans at September 30, 2005. Loans past due 90 days or more, defined as four or more monthly payments in arrears, still accruing interest amounted to \$7.3 million and \$247,000 at September 30, 2006 and 2005 respectively. The increase of loans past due 90 days or more is the result of an increase residential mortgage and consumer past dues of approximately \$6.4 million and \$310,000, respectively. Management considers that the loans in each of the categories are both well-secured and in process of collection. Management reviews the loan portfolio quarterly to identify non-performing credits.

*Deposits.* A primary source for funding our growth is through deposit accumulation. We offer a variety of deposit accounts with a range of interest rates and terms, including savings accounts, checking accounts, money market savings accounts and certificates of deposit. Management is focused on growing our core deposits accounts which include demand, interest checking, savings and money markets as these accounts typically represent low cost deposits. As we develop and grow our core deposit relationships, we have used, and continue to use, the brokered certificate of deposit market to meet loan funding needs. It is management's expectation that core deposit growth will replace a portion of the certificates of deposit as they mature. Additionally, certain products we offer have an element of seasonality; for example, merchant processing volume is greater in the first and fourth quarters and as a result the corresponding deposits are also greater in those periods. To offset the effects of the seasonality, management will use certificates of deposit for funding. At September 30, 2006, we had total deposits of \$1.0 billion as compared to \$732.6 million at December 31, 2005, an increase of \$288.9 million or 39.4%. The following table presents the average balance and rates paid on deposits for the periods indicated:

	For the nine months ended		For the year ended	
	September 30, 2006 Average balance	Average Rate	December 31, 2005 Average balance	Average Rate
Demand (non-interest bearing)	\$ 94,534		\$ 83,921	
Interest checking	59,080	2.34%	27,182	1.14%
Savings and money market	309,216	4.34%	195,805	2.59%
Time	355,995	4.62%	215,243	3.05%



Edgar Filing: Bancorp, Inc. - Form 10-Q

Total deposits	\$ 818,825	3.82%	\$ 554,445	2.29%
----------------	------------	-------	------------	-------

**Borrowings**

At September 30, 2006 we had \$75.0 million in advances from the Federal Home Loan Bank. The advances mature on a daily basis and are collateralized with investment securities and loans. Additionally, we had \$6.2 million in securities sold under agreements to repurchase which also mature on a daily basis.

**Shareholders equity**

At September 30, 2006 we had \$145.4 million in shareholders equity. During the first nine months of 2006 we issued 51,866 shares from the exercise of stock options with net proceeds to us of approximately \$686,000. Cash dividends paid on Series A preferred stock decreased to \$57,000 as a result of our solicitation of the Series A stockholders in 2005 to convert to common shares. We offered a conversion premium of \$.60 per share. Accumulated other comprehensive loss increased \$149,000 due to decreased valuations in our investment portfolio.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

There has been no material change in our assessment of our sensitivity to market risk since our presentation in our Annual Report on Form 10-K for the year ended December 31, 2005 except as set forth in Part I, Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations in this Quarterly Report on Form 10-Q.

**Item 4. Controls and Procedures**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in Securities and Exchange Act of 1934 reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our chief executive officer and our chief financial officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, our management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Under the supervision of our chief executive officer and chief financial officer, we have carried out an evaluation of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based upon that evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures are effective at the reasonable assurance level.

There have been no significant changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially effect, our internal control over financial reporting during our most recent quarter.

**PART II - OTHER INFORMATION**

**ITEM 6. EXHIBITS**

The Exhibits furnished as part of this Quarterly Report on Form 10-Q are identified in the Exhibit Index immediately following the signature page of this Report. Such Exhibit Index is incorporated herein by reference.

Edgar Filing: Bancorp, Inc. - Form 10-Q

---

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

THE BANCORP INC.  
(Registrant)

November 9, 2006  
Date

/s/ Betsy Z. Cohen  
Betsy Z. Cohen  
Chief Executive Officer

November 9, 2006  
Date

/s/ Martin F. Egan  
Martin F. Egan  
Chief Financial Officer and Secretary

Edgar Filing: Bancorp, Inc. - Form 10-Q

---

<b>Exhibit No.</b>	<b>Description</b>
3.1	Certificate of Incorporation <sup>(1)</sup>
3.2	Bylaws <sup>(1)</sup>
10.9	Amended and Restated Sublease Agreement, dated as of June 30, 2006, among The Bancorp, Inc., The Bancorp Bank and RAIT Partnership, L.P.
31.1	Rule 13a-14(a)/15d-14(a) Certifications
31.2	Rule 13a-14(a)/15d-14(a) Certifications
32.1	Section 1350 Certifications
32.2	Section 1350 Certifications

---

(1) Filed previously as an exhibit to our Registration Statement on Form S-4, as amended, registration number 333-117385, and by this reference incorporated herein.